

***United States Court of Appeals
for the Second Circuit***



APPENDIX

ORIGINAL

77-6095

In The
United States Court of Appeals
For The Second Circuit

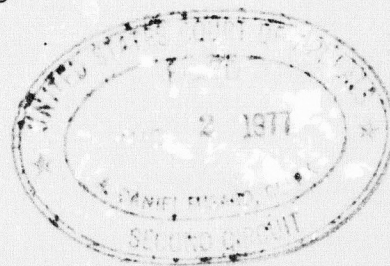
AMERICAN TELEPHONE AND TELEGRAPH COMPANY,
Plaintiff-Appellant,

-against-

THE UNITED STATES OF AMERICA,
Defendant-Appellee.

JOINT APPENDIX FOR APPELLANT

FRANK L. FULLER III
VICTOR S. GOMPERS
Attorneys for Plaintiff Appellant
195 Broadway
New York, New York 10007
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TABLE OF CONTENTS

	Page
Docket Entries	1a
Complaint (Filed February 4, 1976)	3a
Answer (Filed July 7, 1976)	9a
Notice of Motion for Summary Judgment (Filed October 1, 1976)	11a
Affidavit of Cyrus J. Halpern in Support of Motion	12a
Joint Statement Pursuant to Rule 9(g)	18a
Opinion of Carter, J. (Filed April 15, 1977)	24a
Judgment (Filed April 18, 1977)	33a
Notice of Appeal (Dated June 8, 1977)	34a

DOCKET ENTRIES
(pp. 1a-2a)

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Carter

AMERICAN TELEPHONE AND TELEGRAPH CO.

THE UNITED STATES OF AMERICA

wif

Recover of taxes erroneously collected.

CAUSE

FULLER 111 & Gomperts
195 Bway, NYC 10007
393-4321

ATTORNEYS

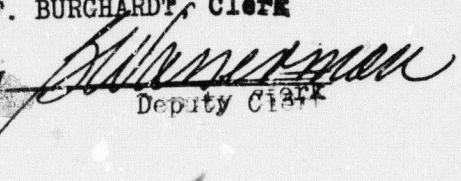
Thomas E. Moseley
Asst. U.S. Atty for Southern
District of N.Y. Atty
One St. Andrew's Plaza
New York, N.Y. 10007
791-9026

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				JS-6	
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UNITED STATES DISTRICT COURT DOCKET

DATE	NR.	PROCEEDINGS
2-1-76		Fld Compl + Iss Summ.
2-19-76		Fld Summs with Marshal ret. Served: by Certified Mail upon Atty Gen Wash D.C. " " Recpt#285504 dtd 2-16-76 U.S.A. by P. Troia on 2-9-76. PRES-TRAIL CONFIDENTIAL BY Carter, J.
4-10-76		Fld Slip & Order tht deft's time to answer the complt is ext to 6-4-76..Carter, J.
6-22-76		Fld Slip & Order that plttf shall serve and file a motion for summ judg by 9-20-76.Carter, J.
7-7-76		Fld ANSWER to the complt. TEM
9-15-76		Fld Slip & Order that plttf's time to file amotion for summjudg is ect to 10-4-76 ---Carter, J.
10-1-76		Fld Pltf's motion for summ judg...ret 11-12-76-10AM Rm 1105.
10-1-76		Fld Plttf Memo support of its motion for summ judg.
10-1-76		Fld Plttf's Joint Statement pur to GEN Rule 9(g).
10-27-76		Fld Slip & Orfer deft shall file its opposition to plttfs' motion for summ judg by 10-29-76...etc....Carter, J
11-9-76		Fld Slip & Order that plttf's motion forsumm jugg is adj to 12-3-76 etc...Cart,erj.
11-26-76		Pl Govt's memo of law in support of its x-motion for summ judg.
12-1-76		Pl Pltf's reply memo in support of motion for summ judg.
4-6-77		Filed transcript of record of proceedings, dated 1-28-77
4-15-77		Fld Opinion#45797-4---Summ judg is gganted in favor of deft. It is so Ordered.....Carter, J' mn
4-18-77		Fld Judgment...Order that deft can have judgment against plttf American Telephone and Telegraph Co dismissing complt....Clerk. mn

A TRUE COPY
RAYMOND F. BURCHARDT, Clerk

By 
Deputy Clerk

COMPLAINT
(Filed February 4, 1976)

(pp. 3a-8a)

3a

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

-----X
AMERICAN TELEPHONE AND TELEGRAPH
COMPANY,

Plaintiff,

-against-

THE UNITED STATES OF AMERICA,

Defendant.

:
Civil Action
: No. 76 Civ.
571 (RLC)

COMPLAINT

-----X
JURISDICTION

1. This civil action is brought under the provisions of Title 28, United States Code, Section 1346(a)(1) and Title 26, United States Code, Section 7422, for the recovery of internal revenue taxes erroneously or illegally collected from the plaintiff by the defendant.

CLAIMS

2. American Telephone and Telegraph Company is a corporation organized under the laws of the state of New York. Its principal executive offices are located at 195 Broadway, New York, New York.

3. American Telephone and Telegraph Company, as the common parent of a group of affiliated corporations, filed with the District Director Internal Revenue, Manhattan, a consolidated United States Federal income tax return for the taxable year 1964.

4. The consolidated tax return was filed, pursuant to extensions of time, on September 15, 1965 and showed a total liability of \$1,368,496,302.03, payment of which was completed with the return.

5. Thereafter, in response to a Statement of Tax Due on Federal Tax Return (Form 3552) issued pursuant to a Revenue Agent's Report dated December 31, 1969, an additional tax of \$2,232,853.15 together with interest of \$619,540.28, or a total of \$2,852,393.43 was paid by plaintiff to the District Director, Manhattan, on February 9, 1970.

6. On February 8, 1972, plaintiff filed a timely claim for refund on Form 843, claiming an overpayment of taxes for the year 1964 in the amount of \$2,852,393.43.

7. On or about March 20, 1973, plaintiff received from the District Director, Manhattan, a supplemental Revenue Agent's Report dated November 8, 1972, which disallowed in part plaintiff's refund claim.

8. On May 17, 1973, plaintiff filed a formal written protest to certain findings in the supplemental Revenue Agent's Report dated November 8, 1972, and requested a hearing before the Internal Revenue Service's Appellate Division of the Regional Commissioner's Office in New York.

9. On or about May 7, 1973, plaintiff received from the District Director, Manhattan, another supplemental Revenue Agent's Report dated April 30, 1973. This report contained for the first time a determination that the foreign tax credit allowed on the consolidated tax return for the taxable year 1964 be reduced by an amount equal to the United States dollar value of a foreign tax refund (based on the rate of exchange at the time of the refund) received by plaintiff in 1972, even though the United States dollar value of said refund exceeded the amount of foreign tax credit allowed on the 1964 tax return with respect to the payment of foreign tax to which the refund applied.

10. On June 6, 1973, plaintiff filed a formal written protest against the determinations made in the

supplemental Revenue Agent's Report dated April 30, 1973, and requested a hearing on the subject before the Internal Revenue Service's Appellate Division of the Regional Commissioner's Office in New York.

11. On or about November 19, 1974, plaintiff received from the District Director, Manhattan, another supplemental Revenue Agent's Report dated October 31, 1974, which made adjustments to certain previously disallowed expenses claimed on plaintiff's consolidated tax return. This supplemental Revenue Agent's Report did not reflect, however, several other issues raised by plaintiff in its claim for refund for the taxable year 1964.

12. On December 9, 1974, plaintiff filed a request for a hearing before the Internal Revenue Service's Appellate Division of the Regional Commissioner's Office in New York with respect to the issues not reflected in the supplemental Revenue Agent's Report dated October 31, 1974.

13. In the course of the Appellate Division conference and subsequent conferences, the protests dated May 17, 1973 and June 6, 1973 were consolidated for consideration because both protests involved issues raised in connection with the 1964 consolidated tax return. As a result of the conferences, the Internal Revenue Service and plaintiff resolved all the issues raised by plaintiff in its refund claim of February 8, 1972. No agreement was reached with respect to the adjustment of plaintiff's foreign tax credit.

14. On or about July 16, 1975, plaintiff received notice from the Regional Commissioner, Internal Revenue Service, North-Atlantic Region, that the report required by § 6405(a) of the Internal Revenue Code had been forwarded

to the Internal Revenue Service's National Office for submission to the Joint Committee on Internal Revenue Taxation.

15. On or about November 4, 1975, plaintiff received notice from the Regional Commissioner, Internal Revenue Service, North-Atlantic Region, that the Joint Committee on Internal Revenue Taxation had taken no exception to the conclusion the Internal Revenue Service reached on plaintiff's income tax case for the year 1964.

16. On or about November 4, 1975, plaintiff received a formal notice from the Regional Commissioner, Internal Revenue Service, North-Atlantic Region, with respect to the refund claim filed by plaintiff on February 8, 1972. The notice allowed \$856,886.45 of plaintiff's total refund claim of \$2,852,393.43. The amount of \$856,886.45 was derived by offsetting the \$1,634,127.24 amount agreed to and allowed with respect to the refund claim by the amount of the foreign tax credit adjustment of \$777,240.79.

17. No issue remains in controversy regarding the remaining amount of \$1,218,266.19 which was disallowed on the refund claim.

18. Plaintiff disputes the Internal Revenue Service's determination that the proper amount of offset is \$777,240.79. It is plaintiff's contention that the proper amount of offset is \$707,859.29.

19. The facts underlying the erroneous offset on which this action rests are in substance as follows: On January 11, 1967, plaintiff received a Notice of Assessment, dated December 23, 1966, from the Canadian Department of National Revenue, representing an assessment against plaintiff of \$763,272.90 (Canadian dollars) tax and \$87,776.35 (Canadian dollars) interest for the year 1964. The assessment

was in respect of the 15% Canadian nonresident tax that the Bell Telephone Company of Canada had not deducted from certain fees paid to plaintiff.

20. Plaintiff paid the assessment on January 23, 1967 and was allowed a foreign tax credit against its United States tax liability for the year 1964 of \$707,859.29, the United States dollar equivalent of the Canadian tax assessment based upon the rate of exchange on day of payment. In addition, plaintiff had accrued other Canadian taxes in 1964 as a result of taxes payable on receipt of taxable dividends and interest. The United States dollar value of these other Canadian taxes was \$269,085.10. Thus, the total foreign tax credit attributable to Canadian taxes paid by plaintiff for the year 1964 was \$976,944.39.

21. In 1972 the Canadian authorities reversed the assessment and refunded to plaintiff on October 26, 1972, all of the assessed tax paid in 1967.

22. At the time of the refund, however, the rate of exchange of United States dollars for Canadian dollars was 1.0183 (rather than .9274, as at the time of payment). Thus, the total refund of \$763,272.90 (Canadian dollars) had an equivalent United States dollar value of \$777,240.79, which is \$69,381.50 more than the foreign tax credit originally allowed with respect to 1964 as a result of the payment of the Canadian tax assessment.

23. As required by § 905(c) of the Internal Revenue Code of 1954, plaintiff notified the Internal Revenue Service on November 6, 1972 of the receipt of the refund.

24. Section 905(c) provides that if any tax paid is refunded in whole or in part, the taxpayer shall notify the Secretary or his delegate, who shall redetermine the amount of the tax for the year or years affected. Section 1.905-3(a) of the regulations provides in pertinent part:

...in case any tax payment credited is refunded in whole or in part, the taxpayer shall immediately notify the Commissioner. The Commissioner will thereupon redetermine the amount of the tax of such taxpayer for the year or years for which such incorrect credit was granted. (Emphasis supplied)

25. The amount of incorrect credit allowed for the year 1964 was \$707,859.29.

26. In calculating the amount of the redetermination by reference to the rate of exchange in effect on the refund date, the Internal Revenue Service eliminated \$69,381.50 of the \$269,085.10 foreign tax credit correctly claimed on the 1964 consolidated tax return as a result of Canadian taxes paid on the receipt of dividends and interest. The additional \$69,381.50 foreign tax credit eliminated by way of offset was totally unrelated to the refunded Canadian tax. The \$69,381.50 merely represents a gain on currency exchange and is properly includible on the consolidated tax return as such in a subsequent taxable year.

27. By virtue of the aforesaid, the United States of America is indebted to plaintiff in the amount of \$69,381.50, with interest thereon as provided by law.

PRAYER FOR RELIEF

WHEREFORE, plaintiff demands judgement against the United States of America in the sum of \$69,381.50 with interest thereon as provided by law, and for the costs and disbursements in this action and for such other relief as to the Court may seem just and proper.

Respectfully submitted,

By Frank L. Fuller III
Frank L. Fuller III

By Victor S. Gompert
Victor S. Gompert

Dated: New York, N.Y.
February 4, 1976

Attorneys for Plaintiff
195 Broadway
New York, N.Y. 10007
393-4321

WGB:lm

9a

ANSWER

(Filed July 7, 1976)

(pp. 9a-10a)

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

AMERICAN TELEPHONE AND TELEGRAPH :
COMPANY, :

Plaintiff, :

ANSWER

76 Civ. 571 (RLC)

-v-

THE UNITED STATES OF AMERICA, :

Defendant. :

Defendant, United States of America, by its attorney,
Robert B. Fiske, Jr., United States Attorney for the Southern
District of New York, for its answer to the complaint:

ONE: Denies paragraph 1 of the complaint, except
admits plaintiff brings this action under 28 U.S.C. § 1346(a)
(1) and 28 U.S.C. § 7422.

TWO: Admits paragraphs 2 and 3 of the complaint.

THREE: Denies knowledge or information sufficient
to form a belief as to the truth of paragraphs 4 through 23,
25 and 26 of the complaint.

FOUR: Paragraph 24 of the complaint is a conclusion
of law which requires no answer.

FIVE: Denies paragraph 27 of the complaint.

FIRST AFFIRMATIVE DEFENSE

SIX: The complaint fails to state a claim upon
which relief can be granted.

WHEREFORE, defendant, United States of America,
requests judgment dismissing the complaint, together with
its costs and disbursements and such other and further
relief as the Court deems just and proper.

Dated: New York, New York

July 7, 1976

Respectfully submitted,

ROBERT B. FISKE, JR.
United States Attorney for the
Southern District of New York
Attorney for United States of
America.

By: Thomas E. Mosley
THOMAS E. MOSLEY
Assistant United States Attorney
Office & Post Office Address:
United States Attorney's Office
One St. Andrew's Plaza
New York, New York 10007
Tel.: (212) 791-9096

TO: FRANK L. FULLER III and
VICTOR S. COMPTON
Attorneys for Plaintiff
195 Broadway
New York, New York 10007

NOTICE OF MOTION FOR SUMMARY JUDGMENT
(Filed October 1, 1976)

11a

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

-----X
AMERICAN TELEPHONE AND TELEGRAPH
COMPANY,

Plaintiff,

- against -

THE UNITED STATES OF AMERICA,

Defendant.
-----X

: 76 Civ. 571 (RLC)

NOTICE OF MOTION FOR
SUMMARY JUDGMENT

SIRS:

PLEASE TAKE NOTICE that upon the complaint, the annexed affidavit of Cyrus J. Halpern, sworn to on September 29, 1976, upon the annexed joint statement pursuant to Rule 9(g) of the General Rules of this Court, and upon all papers and proceedings had herein, plaintiff will move this Court, the Honorable Robert L. Carter, U.S.D.J., in Room 1105, United States Courthouse, Foley Square, New York, New York 10007 on Friday, the 12th day of November, 1976, at 10:00 A.M., or as soon thereafter as counsel may be heard, for an order pursuant to Rule 56(a) of the Federal Rules of Civil Procedure granting summary judgment in its favor on the grounds that there is no genuine issue as to any material fact and, therefore, plaintiff is entitled to judgment as a matter of law.

PLEASE TAKE FURTHER NOTICE that you are hereby requested to serve any and all papers in answer to this motion at least ten (10) days before the return date of this motion.

Dated: New York, New York
October 1, 1976

By

Victor S. Gompert
Victor S. Gompert
Attorney for Plaintiff
American Telephone and
Telegraph Company
195 Broadway
New York, New York 10007
Tel.: (212) 393-4083

AFFIDAVIT OF CYRUS J. HALPERN IN SUPPORT OF MOTION
(pp. 12a-17a)

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

-----X
AMERICAN TELEPHONE AND TELEGRAPH
COMPANY,

: 76 Civ. 571 (RLC)

Plaintiff,

AFFIDAVIT IN SUPPORT
: OF MOTION FOR SUMMARY
JUDGMENT

- against -

THE UNITED STATES OF AMERICA,

:

Defendant.

-----X
STATE OF NEW YORK
COUNTY OF NEW YORK

} ss.:

CYRUS J. HALPERN, being duly sworn, deposes and
says:

1. I am the Director-Federal Taxes of the
American Telephone and Telegraph Company ("American"), a
New York corporation with its principal executive offices
at 195 Broadway, New York, New York, and am familiar with
the matters set forth below. I make this affidavit in
support of American's motion for summary judgment in the
above-captioned matter.

2. American, as the common parent of a group of
affiliated corporations, filed with the District Director
Internal Revenue, Manhattan, a consolidated United States
Federal income tax return on the accrual basis for the
taxable year 1964. American's 1964 taxable year for Federal
income tax purposes was the calendar year 1964.

3. The consolidated tax return for 1964 was filed,
pursuant to extensions of time, on September 15, 1965, and
showed a total liability of \$1,368,496,302.03, payment of
which was completed with the return.

4. American's 1964 tax return, as filed on September 15, 1965, claimed a foreign tax credit of \$269,085.10 for taxes withheld at source in Canada during American's 1964 taxable year. These taxes were withheld, pursuant to Section 109 of the Canadian Income Tax Act, as a result of the payment to American in 1964 of taxable dividends from Bell Canada and Eastern Telephone and Telegraph Company, and taxable interest from Eastern Telephone and Telegraph Company on advances made to it by American. The dividends and interest were taxed under Sections 106(1)(a) and 106(1)(b), respectively, of the Canadian Income Tax Act.

5. On January 11, 1967, American received a Notice of Assessment, dated December 23, 1966, from the Canadian Department of National Revenue, representing an assessment against American of 763,272.90 Canadian dollars tax and 87,776.38 Canadian dollars interest for the year 1964. The assessment was in respect of the 15% Canadian nonresident tax that Bell Canada had not deducted from certain fees paid to American pursuant to a Service Agreement with Bell Canada. Such fee payments were asserted by Canada to be taxable under Section 106(1)(d) of the Canadian Income Tax Act.

6. American paid the assessment on January 23, 1967 and was allowed, as an audit adjustment in a Revenue Agent's Report dated December 31, 1969, a foreign tax credit against its United States tax liability for the year 1964 of \$707,859.29, which represented the value of the Canadian tax assessment in United States currency according to the rate of exchange on January 23, 1967. The rate of exchange of United States dollars for Canadian dollars was .9274 on January 23, 1967.

7. In response to a Statement of Tax Due on Federal Tax Return (Form 3552) issued pursuant to the Revenue Agent's Report dated December 31, 1969, an additional tax of \$2,232,853.15 together with interest of \$619,540.28, or a total of \$2,852,393.43 was paid by American to the District Director, Manhattan, on February 9, 1970.

8. On February 8, 1972, American filed a timely claim for refund on Form 843, claiming an overpayment of taxes for the year 1964 in the amount of \$2,852,393.43.

9. In late 1972 the Canadian authorities reversed their assessment dated December 23, 1966, and refunded to American, on October 26, 1972, all of the assessed tax and interest paid in 1967.

10. On the day of the refund, the rate of exchange of United States dollars for Canadian dollars was 1.0183. Thus, the total tax refund of 763,272.90 Canadian dollars had an equivalent United States dollar value of \$777,240.72, which is \$69,381.50 more than the foreign tax credit originally allowed as an audit adjustment with respect to 1964 as a result of the payment of the Canadian tax assessment.

11. As required by Section 905(c) of the Internal Revenue Code of 1954, American notified the Internal Revenue Service, on November 6, 1972, of the receipt of the Canadian tax refund.

12. On or about March 20, 1973, American received from the District Director, Manhattan, a supplemental Revenue Agent's Report dated November 8, 1972, which disallowed in part American's refund claim which had been filed on February 8, 1972.

13. On or about May 7, 1973, American received from the District Director, Manhattan, another supplemental Revenue Agent's Report dated April 30, 1973. This report contained a determination that the total amount of foreign tax credit allowed for the taxable year 1964 be reduced by an amount equal to the United States dollar value of a foreign tax refund (based on the rate of exchange on the day of refund) received by American in 1972. In so doing, the Internal Revenue Service adjusted downward by an amount of \$69,381.50 the total foreign tax credit originally claimed on the 1964 consolidated tax return.

14. On May 17, 1973, American filed a formal written protest to certain findings in the supplemental Revenue Agent's Report dated November 8, 1972, and requested a hearing before the Internal Revenue Service's Appellate Division of the Regional Commissioner's Office in New York.

15. On June 6, 1973, American filed a formal written protest against the determination made in the supplemental Revenue Agent's Report dated April 30, 1973, and requested a hearing on the subject before the Internal Revenue Service's Appellate Division of the Regional Commissioner's Office in New York.

16. On or about November 19, 1974, American received from the District Director, Manhattan, another supplemental Revenue Agent's Report dated October 31, 1974, which made adjustments to certain previously disallowed expenses claimed on American's consolidated tax return. This supplemental Revenue Agent's Report did not reflect, however, several other issues raised by American in its claim for refund for the taxable year 1964.

17. On December 9, 1974, American filed a request for a hearing before the Internal Revenue Service's Appellate Division of the Regional Commissioner's Office in New York with respect to the issues not reflected in the supplemental Revenue Agent's Report dated October 31, 1974.

18. In the course of the Appellate Division conference and subsequent conferences, the protests dated May 17, 1973 and June 6, 1973 were consolidated for consideration because both protests involved issues raised in connection with the 1964 consolidated tax return. As a result of the conferences, the Internal Revenue Service and American resolved all the issues raised by American in its refund claim of February 8, 1972. No agreement was reached with respect to the adjustment of American's foreign tax credit.

19. On or about July 16, 1975, American received notice from the Regional Commissioner, Internal Revenue Service, North-Atlantic Region, that the report required by § 6405(a) of the Internal Revenue Code had been forwarded to the Internal Revenue Service's National Office for submission to the Joint Committee on Internal Revenue Taxation.

20. On or about November 4, 1975, American received notice from the Regional Commissioner, Internal Revenue Service, North-Atlantic Region, that the Joint Committee on Internal Revenue Taxation had taken no exception to the conclusion the Internal Revenue Service reached on American's income tax case for the year 1964.

21. On or about November 4, 1975, American received a formal notice from the Regional Commissioner,

Internal Revenue Service, North-Atlantic Region, with respect to the refund claim filed by American on February 8, 1972. The notice allowed \$856,886.45 of American's total refund claim of \$2,852,393.43. The amount of \$856,886.45 was derived by offsetting the \$1,634,127.24 amount agreed to and allowed with respect to the refund claim by the amount of the foreign tax credit adjustment of \$777,240.79.

22. No issue remains in controversy regarding the remaining amount of \$1,218,266.19 which was disallowed on the refund claim.

Cyrus J. Halpern
CYRUS J. HALPERN

Sworn to before me this 29th
day of September, 1976

Susan M. Zilinsky
SUSAN M. ZILINSKY
Notary Public, State of New York
No. 30-653039
Qualified in Nassau County
Cert. Filed in New York County
Commission Expires March 30, 1978

JOINT STATEMENT PURSUANT TO RULE 9(g)
(pp. 18a-23a)

18a

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

-----X
AMERICAN TELEPHONE AND TELEGRAPH
COMPANY,

Plaintiff,

- against -

THE UNITED STATES OF AMERICA,
Defendant.

: 76 Civ. 571 (RLC)

: JOINT STATEMENT PURSUANT
: TO GENERAL RULE 9(g)

-----X
Pursuant to Rule 9(g) of the General Rules of this Court, plaintiff American Telephone and Telegraph Company ("American") and defendant United States of America state the following material facts as to which they contend there is no genuine issue to be tried in connection with American's motion for summary judgment for the relief demanded in the complaint in this action.

1. American is a New York corporation with its principal executive offices at 195 Broadway, New York, New York (Halpern Aff., ¶ 1).*

2. American, as the common parent of a group of affiliated corporations, filed with the District Director Internal Revenue, Manhattan, a consolidated United States Federal income tax return on the accrual basis for the taxable year 1964. American's 1964 taxable year for Federal income tax purposes was the calendar year 1964 (Halpern Aff., ¶ 2).

* "Halpern Aff." citations are to the affidavit, sworn to on September 29, 1976, of Cyrus J. Halpern, Director-Federal Taxes of American, which is filed in support of this motion.

3. The consolidated tax return for 1964 was filed, pursuant to extensions of time, on September 15, 1965 and showed a total liability of \$1,368,496,302.03, payment of which was completed with the return (Halpern Aff., ¶ 3).

4. American's 1964 tax return, as filed on September 15, 1965, claimed a foreign tax credit of \$269,085.10 for taxes withheld at source in Canada during American's 1964 taxable year. These taxes were withheld, pursuant to Section 109 of the Canadian Income Tax Act, as a result of the payment to American in 1964 of taxable dividends from Bell Canada and Eastern Telephone and Telegraph Company, and taxable interest from Eastern Telephone and Telegraph Company on advances made to it by American. The dividends and interest were taxed under Sections 106(1)(a) and 106(1)(b), respectively, of the Canadian Income Tax Act (Halpern Aff., ¶ 4).

5. On January 11, 1967, American received a Notice of Assessment, dated December 23, 1966, from the Canadian Department of National Revenue, representing an assessment against American of 763,272.90 Canadian dollars tax and 87,776.38 Canadian dollars interest for the year 1964. The assessment was in respect of the 15% Canadian nonresident tax that Bell Canada had not deducted from certain fees paid to American pursuant to a Service Agreement with Bell Canada. Such fee payments were asserted by Canada to be taxable under Section 106(1)(d) of the Canadian Income Tax Act (Halpern Aff., ¶ 5).

6. American paid the assessment on January 23, 1967 and was allowed, as an audit adjustment in a Revenue Agent's Report dated December 31, 1969, a foreign tax credit

against its United States tax liability for the year 1964 of \$707,859.29, which represented the value of the Canadian tax assessment in United States currency according to the rate of exchange on January 23, 1967. The rate of exchange of United States dollars for Canadian dollars was .9274 on January 23, 1967 (Halpern Aff., ¶ 6).

7. In response to a Statement of Tax Due on Federal Tax Return (Form 3552) issued pursuant to the Revenue Agent's Report dated December 31, 1969, an additional tax of \$2,232,853.15 together with interest of \$619,540.28, or a total of \$2,852,393.43 was paid by American to the District Director, Manhattan, on February 9, 1970 (Halpern Aff., ¶ 7).

8. On February 8, 1972, American filed a timely claim for refund on Form 843, claiming an overpayment of taxes for the year 1964 in the amount of \$2,852,393.43 (Halpern Aff., ¶ 8).

9. In late 1972 the Canadian authorities reversed their assessment dated December 23, 1966, and refunded to American, on October 26, 1972, all of the assessed tax and interest paid in 1967 (Halpern Aff., ¶ 9).

10. On the day of the refund, the rate of exchange of United States dollars for Canadian dollars was 1.0183. Thus, the total tax refund of 763,272.90 Canadian dollars had an equivalent United States dollar value of \$777,240.79, which is \$69,381.50 more than the foreign tax credit originally allowed as an audit adjustment with respect to 1964 as a result of the payment of the Canadian tax assessment (Halpern Aff., ¶ 10).

11. As required by Section 905(c) of the Internal Revenue Code of 1954, American notified the Internal Revenue Service, on November 6, 1972, of the receipt of the Canadian tax refund (Halpern Aff., ¶ 11).

12. On or about March 20, 1973, American received from the District Director, Manhattan, a supplemental Revenue Agent's Report dated November 8, 1972, which disallowed in part American's refund claim which had been filed on February 8, 1972 (Halpern Aff., ¶ 12).

13. On or about May 7, 1973, American received from the District Director, Manhattan, another supplemental Revenue Agent's Report dated April 30, 1973. This report contained a determination that the total amount of foreign tax credit allowed for the taxable year 1964 be reduced by an amount equal to the United States dollar value of a foreign tax refund (based on the rate of exchange on the day of refund) received by American in 1972. In so doing, the Internal Revenue Service adjusted downward by an amount of \$69,381.50 the total foreign tax credit originally claimed on the 1964 consolidated tax return (Halpern Aff., ¶ 13).

14. On May 17, 1973, American filed a formal written protest to certain findings in the supplemental Revenue Agent's Report dated November 8, 1972, and requested a hearing before the Internal Revenue Service's Appellate Division of the Regional Commissioner's Office in New York (Halpern Aff., ¶ 14).

15. On June 6, 1973, American filed a formal written protest against the determination made in the supplemental Revenue Agent's Report dated April 30, 1973, and

requested a hearing on the subject before the Internal Revenue Service's Appellate Division of the Regional Commissioner's Office in New York (Halpern Aff., ¶15).

16. On or about November 19, 1974, American received from the District Director, Manhattan, another supplemental Revenue Agent's Report dated October 31, 1974, which made adjustments to certain previously disallowed expenses claimed on American's consolidated tax return. This supplemental Revenue Agent's Report did not reflect, however, several other issues raised by American in its claim for refund for the taxable year 1964 (Halpern Aff., ¶ 16).

17. On December 9, 1974, American filed a request for a hearing before the Internal Revenue Service's Appellate Division of the Regional Commissioner's Office in New York with respect to the issues not reflected in the supplemental Revenue Agent's Report dated October 31, 1974 (Halpern Aff., ¶ 17).

18. In the course of the Appellate Division conference and subsequent conferences, the protests dated May 17, 1973 and June 6, 1973 were consolidated for consideration because both protests involved issues raised in connection with the 1964 consolidated tax return. As a result of the conferences, the Internal Revenue Service and American resolved all the issues raised by American in its refund claim of February 8, 1972. No agreement was reached with respect to the adjustment of American's foreign tax credit (Halpern Aff., ¶ 18).

19. On or about July 16, 1975, American received notice from the Regional Commissioner, Internal Revenue Service, North-Atlantic Region, that the report required by § 6405(a) of the Internal Revenue Code had been forwarded to the Internal Revenue Service's National Office for submission

to the Joint Committee on Internal Revenue Taxation (Halpern Aff., ¶ 19).

20. On or about November 4, 1975, American received notice from the Regional Commissioner, Internal Revenue Service, North-Atlantic Region, that the Joint Committee on Internal Revenue Taxation had taken no exception to the conclusion the Internal Revenue Service reached on American's income tax case for the year 1964 (Halpern Aff., ¶ 20).

21. On or about November 4, 1975, American received a formal notice from the Regional Commissioner, Internal Revenue Service, North-Atlantic Region, with respect to the refund claim filed by American on February 8, 1972. The notice allowed \$856,886.45 of American's total refund claim of \$2,852,393.43. The amount of \$856,886.45 was derived by offsetting the \$1,634,127.24 amount agreed to and allowed with respect to the refund claim by the amount of the foreign tax credit adjustment of \$777,240.79 (Halpern Aff., ¶ 21).

22. No issue remains in controversy regarding the remaining amount of \$1,218,266.19 which was disallowed on the refund claim (Halpern Aff., ¶ 22).

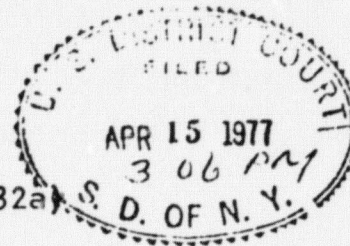
Dated: New York, New York
September 29, 1976.

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OPINION OF CARTER, J.
(Filed April 15, 1977)

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

(pp. 24a-32a)

AMERICAN TELEPHONE AND
TELEGRAPH COMPANY,

Plaintiff,

-against-

THE UNITED STATES OF AMERICA,

Defendant.

76 Civ. 571 (RLC)

45797

A P P E A R A N C E S

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By: THOMAS E. MOSELEY
Assistant United States Attorney

CARTER, District Judge

OPINION

Plaintiff ("ATT") and defendant both move pursuant to Rule 56(a), F.R.Civ.P., for summary judgment. They have submitted a joint 9(g) statement, and there are no material issues of fact to be resolved.

Facts^{1/}

When ATT filed its 1964 federal income tax return, it claimed a foreign tax credit of \$269,085.10 based on its payment of a 15% Canadian income tax on non-residents for 1964. ^{2/} In 1966 Canada made an additional assessment of \$763,272.90 Canadian dollars against ATT for 1964 under the same 15% Canadian income tax of non-residents. ^{3/} Although contesting that assessment, ATT in January, 1967 paid Canada the taxes assessed. On that date the exchange rate was such that the value of ATT's payment was \$707,859.29. ATT claimed this as an additional foreign tax credit, which claim was allowed by the IRS as an adjustment during its audit of ATT's 1964 income tax return. At this point ATT showed a foreign tax credit of \$976,944.39 based on its payment in two parts of the 15% Canadian non-resident tax.

In October of 1972, the Canadian Authorities refunded to ATT \$763,272.90 Canadian dollars -- representing the contested tax assessment against ATT which ATT had paid in 1967. Given the exchange rate at that time, the Canadian refund was worth \$777,249.79, or \$69,381.50 more than the value of ATT's payment to the Canadian authorities in 1967.

Pursuant to Section 905(c) of the Internal Revenue Code, ATT informed the IRS of this refund. The IRS thereupon redetermined ATT's federal income tax due for 1964 by deducting \$777,240.79 from the \$976,944.39 foreign tax credit previously claimed by ATT for 1964.

ATT contests this redetermination, arguing that the IRS should have deducted only \$707,859.29 ^{4/} from ATT's previously claimed foreign tax credit. ATT therefore seeks a refund of \$69,381.50 from the IRS. ^{5/}

Discussion

As I view it, this case is easily determined once the facts are sorted out. Plaintiff having paid a total of \$976,944.39 in taxes to Canada, claimed a foreign tax credit for the same amount on its 1964 adjusted United States income tax return. When Canada refunded \$777,240.79 of the tax it had earlier collected, plaintiff's allowable 1964 foreign tax credit was reduced by the IRS by that amount. This reduction was correctly made pursuant to the applicable sections of the Code.

Section 901(b) of the Code allows a taxpayer to credit against his federal income tax the amount of any income taxes paid to any foreign country. Section 905(c) provides that where there is any subsequent refund of the foreign tax on which a credit was claimed, the Secretary of the Treasury shall "redetermine the amount of the tax for the year or years affected." ^{6/} The issue raised here is how that redetermination shall be made when between the time the foreign tax credit is claimed and a refund is made, there has been a fluctuation in the exchange rate. ^{7/}

The same general issue has been raised previously in other forums and in each case the result has been the same. The redetermination should be made by subtracting from the original foreign tax credit the dollar value of the refund measured at the prevailing exchange rate on the day the refund is made. See S.M. 4747, V-1 C.B. 282 (1926); ^{8/} Rev. Rul. 58-237, 1958-1 Cum. Bul. 534 (1958); ^{9/} Owens, The Foreign Tax Credit (1961) § 7/4B (Rev. Rul. 58-237 is theoretically correct). I see no reason to deviate from these previously reached interpretations of § 905(c) and its predecessors, and I decline to do so. ^{10/}

The opinion might end here, but for the rather interesting argument put forth by plaintiff, which ought not be rejected too easily. Plaintiff concedes that in the ordinary situation the mechanics of redetermination pursuant to Section 905(c) should conform with the Government's interpretation. Plaintiff contends that this is no ordinary situation, however, and that a different result is called for.

As plaintiff views the facts of this case, not one tax was paid, but two — the tax of \$269,085.10 based on §§ 106(l)(a) and 106(l)(b) of the Canadian Income Tax Act, and the tax of \$707,859.29 based on § 106(l)(d) of the Act. ^{11/} This fact, asserts plaintiff, makes the maximum amount the IRS can reduce ATT's tax credit \$707,859.29. Plaintiff reaches this conclusion based primarily on its analysis of Regulation § 1.905-3(a), which ATT argues indicates that the IRS has abandoned its previous interpretation of § 905(c). Reg. § 1.905-3(a) reads:

...[I]n case any tax payment credited is refunded in whole or in part, the taxpayer shall immediately notify the Commissioner. The Commissioner will thereupon redetermine the amount of the tax of such taxpayer for the year or years for which such incorrect credit was granted." (Emphasis supplied by ATT)

ATT reads this regulation as "restricting the redetermination to the amount of the United States tax originally saved due to the taxpayer's claim of an incorrect credit." Pl's. memorandum, at 8. ^{12/} Since \$707,859.29 (the amount paid Canada by ATT in 1967) was the U.S. tax saved by ATT's claim of an "incorrect credit", argues ATT, that is the largest amount by which the IRS may now reduce its 1964 foreign tax credit.

Plaintiff's argument is seriously flawed, however. Reg. § 1.905-3(a) speaks only of a redetermination, following a refund, of a year in which an incorrect credit was granted. It makes no mention of a limit to this redetermination of U.S. taxes "originally saved," and is silent on the question of the proper minuend from which to subtract the refund. It is, therefore, difficult to see why Reg. § 1.905-3(a) should be taken as any indication whatsoever of a change in the administrative interpretation of § 905(c) of the Code.

While I believe the Government's position to be correct and adopt it, it is not amiss to point out what appears to be a sound policy argument to the contrary. The instant and, I believe, correct interpretation of § 905(c) gives to a U.S. taxpayer who has paid a foreign tax which has been credited against his United States tax no incentive to seek any refund from that country, since whatever he receives must be handed over in full to the IRS. The virtue of ATT's proposed reading of § 905(c), on the other hand, is that a U.S. taxpayer would have an incentive to seek refund of a foreign tax since any gain resulting from an exchange rate fluctuation would be taxed only as a capital gain or ordinary income, and the taxpayer would be able to retain some portion of the refund. (In this case while ATT would have to pay the U.S. Government only part of the

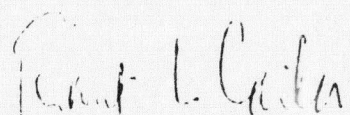
\$69,381.50; it could keep the rest). Were this the rule both the Government and the taxpayer would gain. At present however, a taxpayer has no incentive to seek such a refund, as it is of no import to him, absent unusual patriotic impulses, since he stands to gain nothing for his efforts.¹³ However, these are policy considerations which are the responsibility of the legislature and not the courts to determine.

I think it is also appropriate to note that a difficult problem is presented where the value of the refund exceeds the value of the original foreign tax credit — e.g., if the fluctuation of exchange rates had been such that ATT's refund had been worth \$1,000,000, while its original credit was only \$976,944.39. There is no provision in the Code by which the Government could require the taxpayer to pay over the surplus, and it is difficult to determine how this money should be treated for tax purposes. See Owens, *supra*, ¶ 7/4B at 462, note 64. This problem while a fascinating one, does not arise here, and, therefore, need not be reached to sustain the Government's position.

Since I am bound to read §905 as written, summary judgment is granted in favor of defendant.

IT IS SO ORDERED.

DATED: New York, New York
April 15, 1977



ROBERT L. CARTER
U. S. D. J.

FOOTNOTES

- 1/ Unless specifically stated otherwise, the symbol \$ shall refer to an American dollar, and not a Canadian dollar.
- 2/ These taxes were withheld pursuant to § 109 of the Canadian Income Tax Act, and were based on dividends and interest paid ATT by Canadian companies, which are taxable under §§ 106(l)(a) and 106(l)(b) of the Canadian Income Tax Act.
- 3/ These taxes were assessed pursuant to § 106(l)(d) of the Canadian Income Tax Act, and were based on certain fees paid ATT pursuant to a service contract with a Canadian company.
- 4/ The dollar value of the 1966 Canadian assessment of \$763,272.90 Canadian dollars calculated at the exchange rate when the original payment was made by ATT.
- 5/ $\$777,240.79 - \$707,859.29 = \$69,381.50$
- 6/ Section 905(c) reads in pertinent part:

"(c) Adjustments on payment of accrued taxes. -- If accrued taxes when paid differ from the amounts claimed as credits by the taxpayer, or if any tax paid is refunded in whole or in part, the taxpayer shall notify the Secretary or his delegate, who shall redetermine the amount of the tax for the year or years affected. The amount of tax due on such redetermination, if any, shall be paid by the taxpayer on notice and demand by the Secretary or his delegate, or the amount of tax overpaid, if any, shall be credited or refunded to the taxpayer in accordance with subchapter B of chapter 66 (sec. 6511 and following)."
- 7/ The sequence of events may be summarized as follows:

1964 ATT tax return filed -- \$269,085.10 claimed as foreign tax credit.

1966 additional Canadian assessment -- \$763,272.90 Canadian dollars.

1967 ATT pays assessed taxes -- valued at \$707,859.29.

1969 ATT allowed to adjust foreign tax credit -- \$976,944.39 claimed.

1972 Canada refunds 1966 ATT tax payment -- ATT receives \$763,272.90 Canadian dollars, valued at \$777,240.79.

1973 IRS redetermines ATT's allowable foreign tax credit -- deducts \$777,240.79 from \$976,944.39.

- 8/ Rev. Rul. 68-674, 1968-2 Cum. Bul. 609(1968) declared S.M. 4747 "obsolete". In so doing, the IRS stated that the earlier ruling was not "to be determinative with respect to future transactions." The IRS indicated that part of the reason for declaring the listed rulings obsolete was that they "are now covered by statute, regulation, or later Revenue Rulings." 1968-2 Cum. Bul. 609, 613. That is the case here since Rev. Rul. 58-237 covers the same issue as that involved in S.M. 4747, and indeed the later ruling merely adopts the rationale of the earlier. In Bank of America Nat'l Trust & Savings v. United States, 459 F.2d 513, n.14 (9th Cir.), cert. den., 401 U.S. 271 (1972) it was held that a declaration of obsolescence "does not 'mean that the conclusion or underlying rationale [of the obsolete ruling] has no current applicability'". This court sees the result in S.M. 4747 as only one of several indications that the Government's position is correct.
- 9/ The administrative ruling in S.M. 4747, supra, involved a section of the Revenue Act of 1918, 40 Stat. 1057, which is analogous to § 905(c) of the Code. The ruling in Rev. Rul. 58-237, supra, involved § 131(c) of the Revenue Act of 1939, 53 Stat. 1, which was the equivalent of § 905(c) in that Act.
- 10/ It should be noted that Congress has successively reenacted without change the foreign tax credit adjustment provisions on which these administrative rulings were made. Comprehensive Designers International, Ltd. v. Commissioner, 66 T.C. 348, 355 (Tax Court 1976). This can be taken as concurrence by Congress in the IRS' interpretation, and while not dispositive of the issue here, is a factor to be considered. Helvering v. Reynolds Co., 306 U.S. 110 (1939).
- 11/ Perhaps all that need be said is that ATT's attempt to break-down its payment of 1964 Canadian taxes into two separate sums is at odds with reality. Both the earlier and later tax assessments were made pursuant to Canada's 15 percent non-resident income tax. As such they are certainly fungible. The refund of the 1967 payment should, therefore, be treated no differently than had all of the \$976,944.39 paid Canada have been taxed under the same subsection of the Canadian Income Tax Act and \$777,240.79 been refunded. Other than the fact that in this case the dollar's value diminished between payment and refund, the situation here is not significantly different from the situations involved in S.M. 4747, supra, and Rev. Rul. 58-237, supra. Thus, the result should also be no different.

12/

ATT further claims that the \$69,381.50 gain resulting from the fluctuation of the exchange rate should be treated as a foreign currency gain, and treated according to the dictates of the "tax benefit rule", § 111 of the Code. As the court finds the application of § 905(c) proper in this case, though, it is unnecessary to determine whether the analogy to a foreign currency gain is apt, since § 111 governs the treatment of a refund only to the extent that it is not covered by § 905(c).

13/

Of course even under ATT's proffered interpretation of § 905(c) a taxpayer would have an incentive to seek a refund of a foreign tax paid only when he could expect that the refund, by virtue of a fluctuation in the exchange rate, would be greater than the amount originally paid. How often this would occur, this court does not know.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

Plaintiff

-against-

JUDGMENT

Defendant

ORDERED, ADJUDGED and DECREED: That defendant UNITED STATES OF AMERICA have judgment against plaintiff AMERICAN TELEPHONE and TELEGRAPH COMPANY dismissing the complaint.

Don't do it
Clerk

MICROFILM

APR 19 1977

NOTICE OF APPEAL
(Dated June 8, 1977)

34a

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

-----X

AMERICAN TELEPHONE AND TELEGRAPH
COMPANY,

Plaintiff,

- against -

THE UNITED STATES OF AMERICA

Defendant.

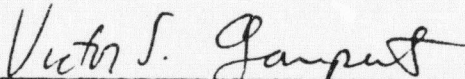
76 Civ. 571 (RLC)

NOTICE OF APPEAL

-----X

Notice is hereby given that American Telephone and Telegraph Company, plaintiff above named, hereby appeals to the United States Court of Appeals for the Second Circuit from the final judgment granting summary judgment in favor of defendant, entered in this action on the 18th day of April, 1977.

Dated: New York, New York
June 8, 1977


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COURT OF APPEALS
SECOND CIRCUIT

AMERICAN TELEPHONE AND TELEGRAPH
COMPANY,

Plaintiff-Appellant,

- against -

UNITED STATES OF AMERICA,
Defendant-Appellee,

Index No.

Affidavit of Personal Service

STATE OF NEW YORK, COUNTY OF

SS.:

I, James A. Steele being duly sworn, depose and say that deponent is not a party to the action,
is over 18 years of age and resides at 112 West 136th Street; New York, New York

That on the 2nd day of J August 19 77 at One St. Andrews Plaza
New York, New York

deponent served the annexed

upon

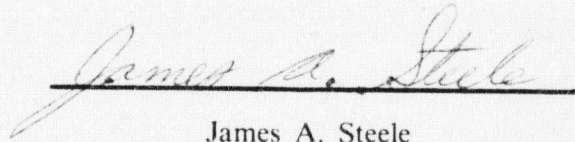
Appendix Brief

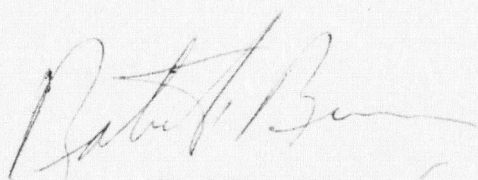
Thomoseley

Thomas Moseley. U.S. Atty.

the in this action by delivering a true copy thereof to said individual
personally. Deponent knew the person so served to be the person mentioned and described in said
papers as the herein,

Sworn to before me, this 2nd
day of Aug. 19 77


James A. Steele


ROBERT T. BRIN
NOTAR: U.S. C. State of New York
No. 31 0418950
Qual ed in New York County
Commission Expires March 30, 1979